

# **Fiscal Services Division**

## **Legislative Services Agency**

### **Fiscal Note**

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HF 2045 - Social Security & Pension Income Tax Phase-out (LSB 5621 HV.2)  
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Fiscal Note Version – Amendment H-8001 to HF 2045

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#### **Description**

House File 2045 provides for a five-year phase-out of income tax on all currently taxable pension and social security income.

Amendment H-8001 strikes the phased-out of income taxes on retirement income and inserts increases in the maximum pension exclusion and the Social Security income taxation thresholds. The pension exclusion is raised to \$7,200 (single) and \$14,400 (joint). The income threshold where Social Security begins to be taxable is increased to \$30,000 (single) and \$38,400 (married).

The amendment also provides for indexing the pension exclusion and the Social Security threshold amounts going forward. This will increase the exclusions and thresholds annually at the rate of inflation.

#### **Background**

Iowa currently excludes the first \$6,000 (single) and \$12,000 (joint) of pension income from taxation. Iowa also excludes 50.0% of Social Security income for all taxpayers. The remaining 50.0% is excluded for taxpayers with total income of less than \$25,000 (single) or \$32,000 (joint). For taxpayers with sufficient income, up to 50.0% of Social Security income is taxable by Iowa.

#### **Assumptions**

This estimate was developed by the Department of Revenue based on actual tax returns of Iowa residents from tax year 2003. To age the information from tax year 2003 forward, the Department of Revenue utilized a trend analysis of the growth in taxable pension and social security income, growth in other forms of income, and the growth in the retirement-age population. The results are first calculated on a tax-year basis, and then converted to a fiscal-year basis by distributing the revenue changes among the categories of personal income tax (withholding, estimate payments, payments with returns, and refunds).

#### **Fiscal Impact**

The change to the pension exclusion and the Social Security threshold, along with the indexation of both, is projected to reduce net General Fund revenue by the following amounts:

- FY 2007: \$10.6 million
- FY 2008: \$26.5 million
- FY 2009: \$31.6 million
- FY 2010: \$36.5 million
- FY 2011: \$40.4 million
- FY 2012: \$44.9 million

As a greater percentage of the Iowa population reaches retirement age and as relatively new sources of pension income continue to mature (Individual Retirement Accounts, 401(k) plans, annuities, etc.), the value of the total exemption is projected to continue to increase in years beyond FY 2012.

Since H-8001 excludes additional retirement income from the Iowa personal income tax, the amendment will also lower the amount of money collected through the local option income surtax. The surtax is calculated as a percentage of State income tax liability. Revenue from the surtax is distributed to school districts implementing the tax.

Approximately 285 Iowa school districts currently have an income surtax. Statewide, the surtax raises an amount equal to approximately 3.0% of total net state income tax collections (\$68.6 million in FY 2005). Applying that percentage to the projected tax reductions listed above provides the following additional reductions in income taxes owed by taxpayers benefiting from the exclusions provided in the amendment.

- FY 2007: \$0.3 million
- FY 2008: \$0.8 million
- FY 2009: \$0.9 million
- FY 2010: \$1.1 million
- FY 2011: \$1.2 million
- FY 2012: \$1.3 million

### **Source**

Department of Revenue

/s/ Holly M. Lyons

January 30, 2006

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The fiscal note and correctional impact statement for this bill was prepared pursuant to Joint Rule 17 and pursuant to Section 2.56, Code of Iowa. Data used in developing this fiscal note and correctional impact statement are available from the Fiscal Services Division, Legislative Services Agency to members of the Legislature upon request.

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